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## Help Protect Your Plan's Financial Integrity

In addition to fulfilling federal reporting requirements, securing a professional audit can help protect your plan's financial integrity and ensure that it will have the funds to pay employees' benefits. An audit can reveal problems your plan may have, and your auditor may suggest ways to improve your plan's controls and operations.

Federal pension law (ERISA) generally requires retirement plans to have an annual audit as part of the Form 5500 return/report process. Independent audits of your plan's financial statements by a CPA can help you fulfill your reporting obligations and avoid costly penalties.

### Most Plans Require Audits

Plans with 100 or more participants at the beginning of the plan year -- so-called "large plans" -- are generally subject to the annual audit requirement. The audit requirement also generally applies to a plan with fewer than 100 participants -- a "small plan" -- unless the plan satisfies certain waiver conditions. A plan may be able to file Form 5500 as a small plan and qualify for the audit waiver if the number of participants covered is between 80 and 120 at the start of the plan year and the plan filed Form 5500 as a small plan for the prior year. We can tell you if your plan needs to be audited.

### What Does an Audit Involve?

Basically, auditors assess whether a plan sponsor is complying with the plan document and Department of Labor (DOL) rules and whether the plan's financial statements comply with reporting standards. The financial and operational aspects the auditor will review may vary to some extent from plan to plan. However, one of the most important processes the auditor will look at is the payroll process. Among the items the auditor will scrutinize are whether:

- o Contributions are consistent with employees' signed deferral elections
- o Contributions have been sent to the right party, received, and credited to the right accounts
- o Contributions were deposited in a timely manner
- o Benefit payments were made in accordance with the plan terms

The auditor also will evaluate your overall payroll process to determine that employees are being paid the proper compensation amount and deferrals are being calculated correctly. *(continued Page 2)*

### this issue

Put a Stop to Plan Leaks P.2  
Offering Catch-Ups P.3  
Access to Investment Advise P.4

*(Continued from Page 1)*

**Other issues an audit addresses include:**

- o The proper valuation of plan investments
- o Plan obligations
- o Issues that may affect the plan's tax status

**Controls Are Examined, Too**

The relevant internal controls within the plan's accounting system are assessed as part of the audit. If the employer outsources certain plan-related functions, the review of internal controls includes functions performed by the third party service provider that affect the plan's financial statements. Providers may have their own "SSAE 16" reports that the plan's auditor can rely on to some extent. The employer, as plan administrator, is still responsible for monitoring the overall process, despite the fact that professionals may have been hired to handle day-to-day administrative functions, such as distribution calculations.

Having written policies for your plan helps the auditor review internal controls more quickly and efficiently by providing a starting point for the review. Having an internal process in place to spot-check controls, correct any errors, and document those checks is also helpful.

**Limiting the Audit's Scope**

Federal law allows the plan sponsor/administrator to limit the scope of the plan's annual audit if banks or insurance companies hold the plan's assets and provide written certifications. We can advise whether limiting the scope of your plan's audit would be appropriate in your situation.

Employers shouldn't overlook the importance of securing a quality plan audit if one is required. Please call our firm if you would like to discuss your plan's auditing needs.

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## **Put a Stop to Plan Leaks**

Offering plan loans can encourage some employees who might not otherwise participate to join and contribute to your 401(k) plan. But you don't want plan participants to view their account as a family emergency fund they can tap for any unexpected expense. This attitude can undermine retirement savings success. You can discourage such behavior by taking steps to counter it.

**Too Many Loans**

When they take a plan loan, many employees reduce their contributions to the plan or stop them altogether. You may be able to decrease requests for plan loans by limiting the number of loans an employee can have outstanding at one time and/or the amount an employee can borrow. Another way to control plan-loan amounts is to prohibit borrowing from employer contributions. By doing so, you send a message to employees that company contributions are for retirement only. Educating employees about the pitfalls of taking a plan loan can also be helpful. And, loan fees might make some employees think twice about borrowing from their plan accounts.

**No Resumption of Contributions After a Hardship Withdrawal**

The problem with hardship withdrawals often isn't the effect of the distribution but, rather, employee inertia in restarting contributions. Plans generally must suspend employee contributions for six months after the withdrawal. As a matter of plan design, you can address this problem by automatically restarting the employee's elective deferrals when the suspension period ends. You might also send messages encouraging employees who made hardship withdrawals to restart their contributions.

**Account Cashouts**

The most harm to future retirement security may come from the failure to roll over cash distributions. Use your employee education program to encourage new employees to directly transfer balances from their former employers' plans to your plan (if it accepts rollovers). And encourage retiring employees and other employees leaving your company to directly transfer or roll over their account balances to an IRA or another employer's plan.



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## Offering Catch-up Contributions

Catch-up contributions give older employees who may not have contributed enough to their employer's 401(k) or other retirement savings plan in earlier years an opportunity to catch up by making higher contributions now.

### Catch-up Basics

To be eligible to make catch-up contributions, an employee must be age 50 or older by the end of the year and must first contribute the maximum allowed deferral to the plan. The maximum is determined by the plan document limits or by certain tax law restrictions. For 2012 (and 2011), an eligible employee can make catch-up contributions of up to \$5,500 to a 401(k), 403(b), or 457 plan and up to \$2,500 to a SIMPLE.

### How Contributions Are Treated

Catch-up contributions are not subject to the dollar limit on annual additions to an employee's plan account. Nor do these contributions have to be counted in your actual deferral percentage (ADP) nondiscrimination testing. In addition, catch-up contributions by key employees are not included as part of the threshold amount that triggers required minimum contributions in a top-heavy plan.

To gain these advantages, you must take care not to misclassify an elective deferral as a catch-up contribution. For example, an employee who simply contributes \$5,500 more than in past years cannot choose to have that amount classified as a catch-up contribution.

### Determining Catch-up Contributions

A plan determines whether elective deferrals are catch-up contributions by comparing the total amount deferred by an employee during the year to the applicable tax law and plan limits. Here are some examples. All of the employees are age 50 or older in 2012.

- o Employee #1 defers \$20,000 to the plan. The \$3,000 contribution in excess of the \$17,000 (in 2012) dollar limit on elective deferrals is treated as a catch-up contribution. If the plan had a lower elective deferral limit, a deferral in excess of that limit would be considered a catch-up contribution.
- o Employee #2 defers \$22,000 to his employer's safe harbor 401(k) plan, and his employer makes a 3% non-elective contribution of \$2,000 to his account, for a total contribution of \$24,000. \$5,000 is considered a catch-up contribution because the employee exceeded the tax law's elective deferral limit by that amount. The non-elective employer contribution doesn't factor into the determination.
- o Employee #3, a key employee, receives a \$50,000 profit sharing contribution from her employer in 2012. She also defers \$5,500 to the plan. Her deferral is a catch-up contribution because the profit sharing and elective deferral contributions, when combined, exceed the 2012 dollar limit on annual additions (\$50,000).

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# Increasing Employees' Access to Investment Advice

The U.S. Department of Labor's (DOL) Employee Benefits Security Administration recently issued a final regulation that should make personalized investment advice available to more plan participants. The regulation allows plan service providers that offer investments to a 401(k) or other defined contribution plan to give investment advice to employees investing in the plan -- including recommending their own funds -- without violating fiduciary rules.

The Pension Protection Act of 2006 created a statutory exemption from the prohibited transaction rules to expand the availability of fiduciary investment advice to plan participants. The new regulation establishes guidelines for the exemption.

## Adding an Advice Arrangement

An investment advice arrangement must be structured in one of two ways to qualify for the fiduciary relief. The arrangement can be provided on a "level-fee" basis, meaning investment fees do not vary based on the investments employees select for their accounts. Alternatively, the advice can be given through the use of a computer model certified as unbiased and as applying generally accepted investment theories by an independent expert. The regulation establishes qualifications and a selection process for the investment expert who must perform the certification.

In addition, the plan sponsor or another plan fiduciary (independent of the investment advisor or its affiliates) must authorize the arrangement. Arrangements also must satisfy several other conditions, including disclosure of the advisor's fees and other information and an annual compliance audit.

The final regulation doesn't affect the DOL's prior guidance on the application of the prohibited transaction rules and existing prohibited transaction exemptions to investment advice arrangements.\*

The DOL estimates that approximately 134,000 defined contribution plans covering 17 million participants and beneficiaries will offer investment advice under the new regulation.

\* For example, guidance in Advisory Opinion Nos. 2011-08A, 2005-10A (Country Trust Bank), 2001-09A (SunAmerica Retirement Markets), and 1997-15A (Frost National Bank).

## Benefit Notes

### New Deadline for Participant Fee Disclosure

The U.S. Department of Labor (DOL) recently issued final regulations on fee disclosures that extend the deadlines for both the fee disclosures service providers must furnish to plan sponsors and the disclosures plan sponsors must provide to participants in 401(k) and similar retirement savings plans. For sponsors of calendar-year plans, the deadline for furnishing participants with initial fee disclosure notices is August 30, 2012. The first quarterly statement (for fees incurred July through September) must be furnished no later than November 14, 2012.

### Get Ready To Report Health Care Costs on W-2s

Larger employers that provide health insurance coverage will have to disclose the cost of coverage on Form W-2 (Wage and Tax Statement), starting with W-2s for 2012 (to be furnished to employees in January 2013). For small employers, reporting is optional for health care coverage provided through at least 2012 or until further IRS guidance is issued. A small employer is one that filed fewer than 250 Forms W-2 for the preceding calendar year. So, for example, an employer that files fewer than 250 Forms W-2 for 2011 would not be subject to the reporting requirement for the 2012 calendar year. Employers that are subject to the reporting requirement for 2012 or that intend to provide the information voluntarily should put procedures in place to collect the necessary data.

### Employer Contributions Make a Comeback

Many companies have restored or plan to restore employer contributions that were suspended or reduced since the beginning of 2008, according to the Plan Sponsor Council of America's 401(k) and Profit Sharing Plan Response to Current Conditions, released in late 2011. Of the 14% of plans that suspended employer matching contributions in the past four years (through October 2011), half have fully restored those contributions. Two thirds of the plans surveyed maintained their matching contributions during the survey period, and 12.1% increased their match or added matching contributions.

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Our firm offers a broad range of employee benefit plan services. If we can be of service to you, please call.

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